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ISRAEL'S ECONOMIC SITUATION

-- ISRAEL HAS THE HIGHEST RATE OF INFLATION IN THE WORLD (133 PERCENT IN 1980) AND COULD FACE SERIOUS BALANCE OF PAYMENTS PROBLEMS AS EARLY AS NEXT YEAR.

-- THESE ECONOMIC DIFFICULTIES ARE CAUSED BY A COMBINATION OF INTERNAL AND EXTERNAL FACTORS: INTERNALLY, THE GOVERNMENT OF ISRAEL'S (GOI'S) ATTEMPTS TO MEET THE COUNTRY'S SECURITY REQUIREMENTS (DEFENSE SPENDING ACCOUNTS FOR ABOUT 30 PERCENT OF GNP) WHILE SUPPORTING AN EXTENSIVE SYSTEM OF SOCIAL WELFARE BENEFITS HAVE PRODUCED VERY LARGE BUDGET DEFICITS WHICH ARE FINANCED BY A COMBINATION OF U.S. AID, OTHER FOREIGN AND DOMESTIC BORROWING, AND CREATING NEW MONEY; EXTERNALLY, ISRAEL HAS BEEN HARD HIT BY ESCALATING OIL PRICES (COMPOUNDED BY THE RETURN OF SINAI OIL FIELDS TO EGYPT) AND INCREASINGLY HEAVY FOREIGN DEBT SERVICE OBLIGATIONS.

-- IN 1980, ISRAEL'S FOREIGN DEBT, OF WHICH 40 PERCENT IS OWED TO THE USG, ROSE TO $17.4 BILLION AND AMOUNTED TO A HIGH 25 PERCENT OF EXPORT EARNINGS; ALTHOUGH ISRAELI OFFICIALS HAVE DENIED RECENT PRESS REPORTS THAT THE GOI PLANS TO ASK THE U.S. TO RESCHEDULE OR FORGIVE SOME PAST DEBTS, THEY ARE LIKELY TO PRESS HARD FOR A LARGER PORTION OF GRANTS IN FUTURE AID PROGRAMS.

-- ON THE POSITIVE SIDE, DURING 1980 THE GOI'S AUSTERITY PROGRAM CONTRIBUTED TO A SUBSTANTIAL INCREASE IN EXPORTS AND A SLOWER RATE OF IMPORT GROWTH; THESE FACTORS REDUCED THE TRADE DEFICIT, AND FOR THE THIRD YEAR IN A ROW ISRAEL HAD AN OVERALL BALANCE OF PAYMENTS SURPLUS.

-- ISRAEL'S ECONOMIC PROSPECTS FOR THE FUTURE ARE UNCERTAIN, AND THE BALANCE OF PAYMENTS SITUATION COULD DETERIORATE THIS YEAR AND NEXT; MUCH DEPENDS ON HOW STRICTLY THE GOI STICKS TO A TOUGH AUSTERITY PROGRAM AND WHAT HAPPENS TO WORLD OIL PRICES.

-- THE BEGIN GOVERNMENT MAY MOVE AWAY FROM ITS CURRENT AUSTERITY PROGRAM AS IT FACES THE JUNE 30 ELECTIONS, WHICH COULD EVENTUALLY LEAD TO MORE INFLATION AND A WORSENING BALANCE OF PAYMENTS.

-- NEVERTHELESS, THE $2.185 BILLION FY 1982 AID PACKAGE PROPOSED FOR ISRAEL SHOULD BE ENOUGH TO MEET ISRAEL'S ESSENTIAL MILITARY AND ECONOMIC REQUIREMENTS FOR THAT YEAR BARRING AN UNEXPECTED DETERIORATION IN ISRAEL'S ECONOMIC SITUATION.